Supreme Court, U.S.
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No. 95-1511

In The

Supreme Court of the United States

October Term, 1995

JOHN L. KEMMERER and
JAMES L. JORDAN,

Petitioners,

v.

ICI AMERICAS INC.,

Respondent.

On Petition For A Writ Of Certiorari To The United States Court Of Appeals For The Third Circuit

RESPONDENT'S BRIEF IN OPPOSITION

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RULE 29.6 CORPORATE AFFILIATION STATEMENT

Respondent, which was previously known as ICI Americas Inc., changed its name to Zeneca Inc. during the pendency of this litigation. Respondent has two non-wholly owned subsidiaries, Corpus Christi Global Chemicals Company and Image Polymers Company. Zeneca Inc. is ultimately owned 100% by Zeneca Group PLC, a publicly-traded company.

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RESPONDENT'S BRIEF IN OPPOSITION

Respondent ICI Americas Inc. (referred to hereinafter as "ICI")[1] respectfully requests that this Court deny the petition for writ of certiorari seeking review of the Third Circuit's opinion in this case.[2] The decision below is not inconsistent with existing federal law, nor does it reflect a split of authority among the Circuits.

COUNTERSTATEMENT OF THE CASE

This Counterstatement of the Case supplements Petitioners' Statement of the Case, which omits certain important facts.

Petitioners imply, as they did at the trial of this case, that ICI's purpose in terminating its Executive Deferred Compensation Plan ("the Plan") was to achieve an economic gain for ICI, in derogation of the rights and interests of Plan participants. The evidence and the District Court's findings were to the contrary.

The principal reason for the Plan termination was to protect participants from the risk of a default by ICI. In the months preceding the termination, ICI was the subject of a hostile takeover attempt. ICI's senior management

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[1] After the commencement of the litigation, ICI changed its name to Zeneca Inc. For purposes of convenience and consistency, Respondent is identified in this Brief as "ICI."

[2] The Third Circuit's opinion is reported at 70 F.3d 281. The opinions of the United States District Court for the Eastern District of Pennsylvania are unreported. ICI will reference these decisions by citing to Petitioners' Appendix.

recognized that some participants might lose some of the projected benefits of tax deferral as a result of the Plan termination, but they decided that these risks were outweighed by the desirability of distributing the account balances on an accelerated basis. The accelerated distributions protected Petitioners and others from the risk of continuing to participate in an unfunded plan at a time of great uncertainty. The District Court agreed that the decision to terminate the Plan

> was in part motivated by concerns about the security of participants in the [Plan], which concerns increased in mid 1991 when rumors of a hostile takeover of defendant were reported. Terminating the Plan and fully paying [Plan] participants provides the greatest protection against any future happenings which would render defendant incapable of making payments under the [Plan].

(Pet. App. 19a). The District Court did not identify any other reasons for the Plan termination.

More importantly, whatever potential tax and investment losses were contemplated before the Plan was terminated, several developments beginning in 1992 turned such potential losses into gains. First, personal income tax rates for wealthy Americans were raised substantially, effective January 1, 1993. Focusing on Petitioner James Jordan ("Jordan"), as Petitioners have done, reveals the dramatic impact of these changes. The Plan termination resulted in accelerated distributions to Jordan of roughly two-thirds of his account balance in 1991, at a time when the maximum personal income tax rate was thirty-one percent. Had Jordan remained a participant in the Plan,

taking gradual distributions through the year 2007 as he had originally elected, any distributions made after January 1, 1993 would have been taxed at a 39.6 percent rate.

Second, as a result of the Plan termination, the retired participants received a rate of return that substantially exceeded the returns that they would have received under the Plan. After the Plan was terminated, account balances were distributed in three roughly equal installments, beginning in January 1992 and ending in January 1994. During this two-year distribution period, participants were credited with a ten percent annual rate of return on their remaining account balances. Over the same period, however, the returns that would have been available under the Plan were substantially lower, due to low interest rates, and poor performance in the stock and bond markets. Jordan, for example, earned at least $250,000 more on his account balance during the two-year distribution period than he would have earned as a Plan participant.

After consideration was given to these developments, and after correcting flawed assumptions by Petitioners' experts about the rates of return that might have been achieved prospectively in the Plan, ICI's experts demonstrated that as a result of the Plan termination, Petitioners Jordan and Kemmerer achieved **economic gains** in the amounts of $478,000 and $43,966, respectively. Additionally, Petitioners received considerable benefits from the accelerated distributions which were not easily quantifiable, including increased investment liquidity, greater flexibility in estate planning, avoidance of the risk of default and an unlimited number of investment vehicles.

These factors, together with flaws in the model constructed by Petitioners' expert witnesses at trial, prompted the District Court to conclude that Petitioners had not established that they were damaged as a result of the Plan termination. It also explains why Petitioners were the only two of sixty-four retired Plan participants to seek judicial relief from the accelerated distributions.

REASONS WHY THE PETITION SHOULD BE DENIED

I. This Case Does Not Present Issues Warranting The Grant Of Certiorari.

In seeking certiorari, Petitioners attempt to portray the Third Circuit's decision as resting on two narrow legal holdings: 1) whether "damages for the loss of the benefits of tax deferral [are] too speculative to be recoverable because they necessarily depend on unpredictable future tax rates"; and 2) whether "such damages [are] too speculative to be recoverable because at some hypothetical future time the employer might not have been financially able to make the promised deferred compensation payments." (Petition for Writ of Certiorari at i). As shown below, however, neither of the "holdings" which Petitioners present for review actually formed the basis for the Third Circuit's decision. Rather, in a fact-bound review of unique circumstances, the Third Circuit determined simply that the District Court's findings on damages were not "clearly erroneous." Pet. App. 15. Contrary to Petitioners' assertions, no "new law" was created by that decision, and no conflict between the Circuits has

developed. Therefore, for the reasons explained below, the Petition for Writ of Certiorari should be denied.

A. The Third Circuit's Approach To Calculating Potential Damages From Lost Tax Deferral Was Reasonable And Wholly Consistent With Existing Law.

According to Petitioners, the Third Circuit determined as a matter of law that projections as to future tax rates were "too speculative" to support a recovery of damages for tax losses. Even a cursory reading of the Third Circuit's opinion, however, reveals that the Court arrived at no such blanket legal conclusion. Rather, in upholding the District Court's fact-specific determinations, the Third Circuit agreed that, based on the entire factual record before it, Petitioners had not met their burden of proving actual damages.

The record on appeal provided more than sufficient evidence to support the Third Circuit's conclusion that Petitioners failed to prove their claim for actual damages. As noted above, the record evidence demonstrated that Petitioners had actually reaped economic gains from the early termination of the Plan. In part, this was because the maximum federal income tax rate had increased dramatically during the Petitioners' retirement, from thirty-one percent to 39.6%. By accepting accelerated distributions of their benefits while tax rates were at near historic lows, Petitioners greatly minimized their tax burdens.

The Third Circuit found this to be probative of Petitioners' lack of damages, stating as follows:

> [A]s ICI properly points out, by virtue of the plan termination the appellants' account balances were taxed at a much lower rate than would have been the case had payments been made several years later.

Pet. App. 14.

The speculative nature of projecting future tax rates, moreover, was only *one factor among many* that led the Third Circuit to conclude that Petitioners had failed to prove damages. As the Circuit Court specifically noted, "the tax consequences of the accelerated payments were simply part of a larger picture including investment rates of return which the district court concluded did not establish that appellants had suffered or would suffer any financial loss as a result of the acceleration of payments."[3] (*Id.*). The other factors militating against an award of damages included Petitioners' failure to seek immediate injunctive relief, failure to account for "the risk involved in keeping money in an unfunded plan," and failure to prove "that they incurred management fees and transactions costs as a result of the breach." (*Id.*).

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[3] Regarding the "investment rate of return," ICI's expert demonstrated at trial that Petitioners' projected rates of return were grossly inflated. The District Court credited ICI's expert on this point which, both sides acknowledged, was critical to the damages model. Since Petitioners did not provide any alternative damage calculations using different rates of return, it is obvious that the District Court could not have granted the relief which they requested without engaging in speculation.

Petitioners distort the Third Circuit's analysis by seizing a single sentence from the opinion and exaggerating its impact. The Third Circuit's passing comment about future tax rates was not the basis for the Court's holding in this case. Indeed, it was only one of many factors that prompted the Third Circuit to conclude that Petitioners' case was based on "utterly speculative damages."

Try as they might, Petitioners cannot transform an isolated statement into a split of authority between the Circuits. The Third Circuit did not reject the analysis in *Oddi v. Ayco Corp.*, 947 F.2d 257, 261-62 (CA7 1991). Rather, the Third Circuit's decision rests on its sensible conclusion that the District Court's factual findings as to damages were not "clearly erroneous," Pet. App. 15 – a well-reasoned, fact-bound determination that does not merit review by this Court. ICI respectfully requests, therefore, that the Petition for Certiorari be denied.[4]

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[4] ICI must also note that a strong alternative basis exists to support the Third Circuit's decision. At the trial and appellate levels, ICI argued that the damages sought by Petitioners constituted extracontractual damages, which are not recoverable under 29 U.S.C. § 1132(a)(1)(B) or 1132(a)(3). The Third Circuit stated "We are inclined to agree with ICI . . . [b]ut be that as it may, we decline to resolve such intricate issues of ERISA law because appellants failed at trial to prove they were damaged at all." Pet. App. 12. Given this alternative basis for affirmance, Petitioners would be unlikely to prevail in this action even if they could convince this Court that the Third Circuit's decision was otherwise erroneous.

B. The Lower Court's Consideration Of A Risk Premium For Unfunded Pension Benefits Was Not Erroneous.

Petitioners inaccurately characterize the "risk premium" that was accepted by the District and Circuit Courts. They argue that ICI used the risk premium to reduce the damages award, much like a discount rate is used to reduce a future sum to present value. Each of the cases which they cite, including this Court's decision in *Jones & Laughlin Steel Corp. v. Pfeifer*, 462 U.S. 523, 537 (1983), involves the rather mechanical task of discounting future damages to present value.

Petitioners' argument reflects a fundamental misunderstanding of the risk premium. The risk premium was not used to discount future damages. It was used to value alternative forms of assets or benefits, just as it is used routinely in the financial markets, in order to determine whether Petitioners were *damaged at all* by the early distributions of their account balances.

All corporate debt – like ICI's unfunded obligation to make future distributions to Plan participants – carries some risk of default. Debt issued by the largest and most financially secure corporations carries a relatively modest premium, which is measured by the difference between the interest rate paid on the bond, and the interest rate paid by the United States government on treasury securities bearing comparable maturity dates. Financially troubled companies must pay a larger premium – in the form of a higher rate of return – to attract investors, who would not purchase such securities if they did not receive enhanced compensation for the additional risk associated

with such debt. The size of the risk premium varies depending on the magnitude of the risk of default.

Professor Jeremy Siegel, a distinguished professor at the Wharton School of the University of Pennsylvania, explained how the risk premium applies to this case. As he testified, the determination of whether Petitioners incurred any damages at all required the valuation of two alternative forms of benefits: the first, a long-term distribution from general corporate assets under the Plan and, the second, an accelerated distribution upon the Plan termination. The first alternative bore some risk of default by ICI. The second alternative, however, was risk-free, *i.e.*, there was no risk of a future default by ICI. Using published ratings of debt from services such as *Moody's* and *Standard & Poor's*, Professor Siegel developed a risk premium that the marketplace would have used in valuing the unfunded debt by ICI to Plan participants. That risk premium was one of a number of factors, including assumptions relating to rates of return and tax rates, which were then incorporated into an economic model. That model, as explained by ICI's other expert, Mr. Schaefer, showed that Petitioners' economic positions were enhanced considerably as a result of the Plan termination.

Petitioners' argument, therefore, misses the point. Their case is not analogous to a hypothetical automobile accident case, in which future medical expenses and lost wages must be reduced to present value. It is also unlike the typical breach of contract action, in which a party fails to pay an amount that is owed. Here, the Plan accounts were distributed fully. The issue at trial was not

the discounting of the unpaid pension benefits themselves, but the valuation of alternative forms of payment of those benefits in full. The courts below opted for a methodology which incorporated principles that are used universally in the financial markets. There was no error in adopting such a methodology, nor have Petitioners cited cases from any other Circuits which suggest that market value is an inappropriate measure in conducting a valuation of this nature.

In fact, this Court has recognized that risk is an appropriate factor to be considered in valuing an asset. In *Kimball Laundry Co. v. United States*, 338 U.S. 1 (1949), an owner of a laundry challenged the compensation that was provided by the government when the facility was temporarily condemned for use by the military. The Court noted that in valuing the business as a going concern, a purchaser would measure the probable return upon investment by capitalizing such returns "at a rate *taking into account the element of risk* and the number of years during which these factors would probably have effect. . . ." 338 U.S. at 17 (footnote omitted) (emphasis added). The opinion in *Kimball Laundry* has been cited for the proposition that the "estimation of risks is part of the business of valuation." 1 Dan Dobbs, *Law of Remedies: Damages-Equity-Restitution* § 3.5, at 332 n.54 (2d ed. 1993).

Petitioners do not deny that risk is appropriately considered in valuing assets or forms of benefits. Nevertheless, they omitted this important variable from their expert's analysis. This failure in Petitioners' model left the District Court to speculate as to the comparative

values of the alternative distribution methods. The District Court and the Third Circuit prudently declined to engage in such speculation. Petitioners should not be granted Certiorari to remedy their own evidentiary shortcomings.

CONCLUSION

For these reasons, the petition for a writ of certiorari should be denied.

Respectfully submitted,

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